

**INTERNAL REVENUE SERVICE
ADVISORY COUNCIL**

REPORT TO THE COMMISSIONER

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**GENERAL REPORT
OF THE
INTERNAL REVENUE SERVICE
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INTRODUCTION

The purpose of the Internal Revenue Service Advisory Council (hereinafter “IRSAC” or the “Council”) is to provide an organized public forum for discussion of relevant tax administration issues between Internal Revenue Service (hereinafter “IRS” or the “Service”) officials and representatives of the public. For fiscal year 2003, membership on the IRSAC consisted of twenty-three individuals who bring a wide breadth of experience, disparate expertise, and diverse backgrounds to bear on the Council’s activities.

The IRSAC has organized itself into three subgroups, corresponding to three of the four IRS’ Operating Divisions: the Large & Mid-Size Business Subgroup (hereinafter the “LMSB Subgroup”); the Small Business & Self-Employed Subgroup (hereinafter the “SBSE Subgroup”); and the Wage & Investment Subgroup (hereinafter the “W&I Subgroup”). Each Subgroup has issued a report that follows the general report of the entire IRSAC. All reports are a result of working sessions held in Washington during the year and numerous conference calls between IRSAC members and key IRS personnel. If not for the hard work of IRSAC members and the cooperation and efforts of representatives of the Service this report would not have been possible. We must offer special thanks to the staff of the Office of National Public Liaison for ensuring that IRSAC had all resources necessary to perform its advisory function.

ISSUE ONE: COMMUNICATION

Each year, the IRS gathers a great deal of information that in turn, it tries to communicate to both taxpayers and stakeholders. Effective communication increases stakeholder and taxpayer knowledge of the tax law and thus, increases their ability to successfully comply with the law and meet their compliance obligations. This suggests that effective communication ultimately gives rise to increased compliance. The Service utilizes many methods by which it attempts to communicate to stakeholders. Some of these methods: are stakeholder meetings; the IRS Web site; workshops, and the Nationwide Tax Forum Program. Although we commend the Service for its efforts, we are concerned that some messages do not reach the majority of the intended audience.

The IRSAC again attended the IRS Nationwide Tax Forums (hereinafter "Forums") during fiscal year 2003, partnering with members of the Information Reporting Program Advisory Committee (hereinafter "IRPAC") to conduct focus groups (hereinafter "Focus Groups") in Atlantic City, Atlanta, San Antonio, and Las Vegas. With upwards of 16,000 practitioners attending, we believe the Forums represent the best vehicle through which the IRS can reach practitioners as regards issues of importance. The IRSAC and IRPAC Focus Groups are intended to develop an understanding of issues that bear on practitioners, and to gauge the level of taxpayer/practitioner awareness as regards programs that impact these stakeholders in the ordinary course of their daily activities. We were disappointed to discover how little was known about programs such as the National Research Program and changes in the Offer in Compromise Program along with many other topics. We also found that the participants preferred smaller groups as they permit greater in depth discussions regarding topics of which they previously had little knowledge. If not for these Forums,

practitioners might not have received this necessary, additional information, contrary to the assumption of many Advisory Group members. The IRSAC believes that the Forums are a major tool that should be utilized to educate the practitioner community. The IRSAC also suggests that the Service continue to use such groups as the IRSAC and IRPAC to get their message out.

It was more difficult to determine the effectiveness of the IRS Web site. The IRSAC understands that those using the Web site found it much improved and very helpful. It was more difficult to judge however, how many practitioners actually use the Web site. Continued education provided by the Forums and other methods should be implemented to increase awareness of the benefits provided by the IRS Web site.

ISSUE TWO: INTERNAL REVENUE SERVICE BUDGET & WORKLOAD

For many years the IRSAC has recommended that the IRS receive adequate funding to implement its difficult tasks. We again reiterate our belief in the need for the IRS to receive adequate funding to operate effectively. However, the IRSAC believes that past budget issues faced by the IRS may be small compared to those the Service may potentially face in the coming years. The reality is that workloads are increasing and resources have not increased correspondingly. The Service has sought and continues to seek ways to improve service, increase enforcement, add new technology, and reduce taxpayer burden in the face of limited resources. The IRSAC commends their efforts and encourages the Service to continue performing all these important tasks. Unfortunately, without adequate funding, the IRSAC is concerned that both taxpayers and the tax system will suffer.

Tight budgets demand difficult decisions. One of these decisions may be to choose between taxpayer service and an increase in enforcement. As you will read in the reports of

our subgroups, the IRSAC is concerned that taxpayers have become more aggressive in taking chances as regards tax obligations and more willing to engage in the audit lottery. Practitioners we talked to in our Focus Groups verified this change in taxpayer attitude. In deciding how to prioritize IRS functions, the IRSAC believes that an effort must be made to enhance enforcement and begin insuring taxpayers that all taxpayers are being treated equally and that all are paying their fair share. The IRSAC commends Commissioner Everson for recognizing the need to find the proper balance between service and enforcement. However, the IRSAC must offer a word of caution; for many external stakeholders, talk of enhanced enforcement gives rise to the fear that the IRS will return to its old ways of doing business which created so many problems only a few years ago. The IRSAC recommends that the words and actions of the Service necessarily insure that enhanced enforcement will be a step forward not a leap back.

Limited resources have also forced the IRS to look for different ways to approach compliance problems. An example of this new thinking is the Offshore Voluntary Compliance Initiative and LMSB's Limited Issue Focus Exam Program. In these cases, the Service faced significant compliance problems that could not be addressed in traditional ways. These problems not only required attention, but a realization that budget issues required a solution that took into account the reality of limited resources. To date, the approaches taken by the Service in these areas have been successful and hopefully will serve as an example that new thinking can lead to new ways to address old problems. The IRSAC feels that in these times of tight budgets, all Operating Divisions must be challenged to create new, more efficient programs geared to improve compliance and enforcement.

ISSUE THREE: THE INTERNAL REVENUE SERVICE ADVISORY COUNCIL AND STAKEHOLDER INVOLVEMENT

Last year, a decision was made to extend IRSAC membership from two to three year terms. This decision was made to provide the IRSAC with greater continuity by replacing one third of its members each year. The IRSAC believes that the timing of this change was appropriate as it permitted experienced IRSAC members to be in place when the new Commissioner was confirmed. The IRSAC also feels that this change will allow the IRSAC to begin work immediately each year as the majority of its members and the leadership will be in place with people who have been involved with the Council for no less than one year.

The IRSAC is representative of many outside stakeholders and stakeholder groups upon whom the IRS depends for crucial feedback and/or input. During our tenure, the members of the IRSAC have seen outside input utilized to advantage and ignored to the disadvantage of the Service. Unfortunately, there appears to be no consistent approach or infrastructure in place in the Service to determine how best to utilize outside stakeholders. It appears to the IRSAC that the use of outside stakeholders is determined more on a person-by-person basis rather than as an agency-wide acceptance strategy. The IRSAC believes that until the entire IRS is comfortable partnering with and utilizing outside stakeholders, a huge resource and sounding board will remain untapped. The K-1 matching program is a perfect example of our concerns.

The IRSAC, along with other outside stakeholder groups, issued warnings early in the K-1 Matching Program design regarding problems that could be faced if the Service implemented a program without input from outside stakeholders. Unfortunately, these suggestions were ignored and the K-1 Matching Program was launched with dismal results. Ultimately because of many complaints from taxpayers, practitioners, other outside

stakeholder groups, and Congress, the program was stopped. This expensive and embarrassing mistake could have been avoided. The Service also failed to consult adequately with the Wage and Investment Subgroup and other stakeholders on two important topics: (i) the EITC Pre-certification initiative; and (ii) the revamping of ITINs. To the IRS's credit, however, they took the opposite approach in the design of the new K-1 Matching Program that launched this year. After much consultation with outside stakeholders, a modified program has begun that appears to be much more effective, and less burdensome on taxpayers. A more detailed discussion of this new program appears in the Small Business Self Employed Subgroup Report that follows this General Report.

We were also made aware of another example of how the use of outside stakeholders could provide the Service with additional benefits. In our presentations at the Forums, we discussed the EITC pre-certification program mentioned above. We found that many practitioners were willing to voluntarily pre-certify their clients if possible. By using practitioners in this manner, additional taxpayers would pre-certify with little or no additional cost to the Service. Further, because additional practitioners would be part of the process, their input could go a long way toward developing a program for use by all effected taxpayers which would therefore increase enforcement in a meaningful way.

The IRSAC hopes this perspective will serve as an example of how the use of outside stakeholders can be beneficial to the Service and ultimately to the taxpayers we all serve. We also hope that use of outside stakeholders will become consistent at all levels and in all IRS Operating Divisions.

CONCLUSION

This year's Council worked through the transition from Commissioner Rossotti to Commissioner Everson. We look forward to our continuing relationship with Commissioner Everson. We are in agreement with the goals and priorities he has set for the Service in the coming years. The IRSAC hopes that by working with Commissioner Everson and each of the business operating divisions we can contribute to achieving those goals.